SUGGESTED ANSWERS

PROFESSIONAL PROGRAMME

CORPORATE RESTRUCTURING, VALUATION AND INSOLVENCY
(PP-CRVI /2013)

THE INSTITUTE OF
Company Secretaries of India
IN PURSUIT OF PROFESSIONAL EXCELLENCE
Statutory body under an Act of Parliament
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These answers have been written by competent persons and the Institute hopes that the SUGGESTED ANSWERS will assist the students in preparing for the Institute's examinations. It is, however, to be noted that the answers are to be treated as model and not exhaustive answers and the Institute is not in any way responsible for the correctness or otherwise of the answers compiled and published herein.

The Suggested Answers contain the information based on the Laws/Rules applicable at the time of preparation. However, students are expected to be well versed with the amendments in the Laws/Rules made upto six months prior to the date of examination.
Question No. 1

State whether the following statements are true or false citing briefly relevant provisions of the law:

(i) Provisions of the Specific Relief Act, 1963 override the provisions of sections 391 and 392.
(ii) A non-profit making company licensed under section 25 can be merged with a profit making company.
(iii) High Court can sanction a scheme of merger of a sick industrial company when a revival scheme is pending before BIFR.
(iv) Court cannot refuse to sanction a scheme of arrangement which has been approved by majority of shareholders/creditors of the companies concerned.
(v) Court would not insist on prior approval of stock exchange(s) while sanctioning a scheme of arrangement.
(vi) The word ‘amalgamation’ or ‘merger’ is not defined anywhere in the Companies Act, 1956.
(vii) Amalgamation between two banking companies is governed solely by the Companies Act, 1956.

(2 marks each)

Answer to Question No. 1(i)

False

Provisions of the Specific Relief Act, 1963 does not override the provision of section 391 & 392 of the Companies Act, 1956. In case of Divya Vasundhara Financier Limited v. KN Samant (1990) 69 Comp. Cases, it was held that the Court while passing a scheme of arrangement under section 391 can also pass order of eviction against a person who prima facie does not have any right, title or interest in the property by issuing suitable directions.

Answer to Question No. 1(ii)

True

Amalgamation of a company licensed under Section 25 of the Companies Act with a commercial, trading or manufacturing company could be sanctioned under
Section 391/394. [Re: Sir Mathurdas Vissanji Foundation (1992) 8 CLA 170(Bom.) Re: Walvis Flour Mill Company P. Ltd. (1996) 23 CLA 104]. There need not be unison or identity between objects of Transferor Company and Transferee Company. Companies carrying entirely dissimilar businesses can amalgamate. [Re: PMP Auto Inds. Ltd. (1994) 80 Comp. Case 291 (Bom.)].

Answer to Question No. 1(iii)

False

In the matter of Tata Motors Ltd. v. Pharmaceuticals Products of India Ltd. and Another (2008) 144 Comp. Case 178 (SC), the Supreme Court held that the High Court cannot sanction scheme proposed under section 391/394 of the Act during the pendency of the revival scheme before BIFR under SICA. In terms of Section 26 of SICA, a company court did not have jurisdiction to entertain any application of a sick industrial company for merger under Section 391 to 394 of the Companies Act 1956, while the matter was pending before the BIFR or the AAAIFR. Similarly in Ashok Organic Industries Ltd. v. ARCIL, [2008]114 Comp Cas 144 (Bom), the Bombay High Court held that once the Industrial Company makes a reference under Section 15 of the SICA, the Company Court would have no jurisdiction for sanctioning the scheme of arrangement of compromise with its creditors and shareholders and neither will it have jurisdiction to take cognisance of such an application during the pendency of the reference.

Answer to Question No. 1(iv)

True

When a scheme of compromise/arrangement is sound not opposed to public policy and does not violate any law/statute and nature justice and is supported by majority of shareholders/creditors, the Court would sanction the scheme under Section 391 of the Companies Act, 1956.

Answer to Question No. 1(v)

True

However, pursuant to Clause 24 of the Listing Agreement, all listed companies shall have to file scheme/petition proposed to be filed before any Court/Tribunal under Sections 391, 394 and 101 of Companies Act, 1956, with the Stock Exchange, for approval, at least a month before it is presented to the Court or Tribunal.

Answer to Question No. 1(vi)

True

The word ‘amalgamation’ or ‘merger’ is not defined anywhere in the Companies Act, 1956. However Section 2(1B) of the Income Tax Act, 1961 defines ‘amalgamation’.

Answer to Question No. 1(vii)

False

Amalgamation of one banking company with another banking company is governed by the provisions of Banking Regulation Act, 1949. Section 44A of the Banking Regulation Act, 1949 provides for procedure of amalgamation of two banking companies.
Question No. 2

(a) In a scheme of arrangement made under section 391, a company proposes to transfer one of its undertakings to its subsidiary and also to reduce its share capital. Is the scheme valid? Explain with relevant provisions of law and relevant cases.

(b) Explain the provisions relating to buy-back of shares through book-building route.

Answer to Question No. 2(a)

Yes, the scheme is a valid scheme and is well within the scope of Section 391 read with Section 394 of the Act. In the case of Larsen & Toubro Limited In re [2004] 60 CLA 335 (Bom) [2004], the Mumbai High Court held that a composite scheme could be made involving de-merger, of one of the undertakings of the transferor company and for the transfer of the demerged undertaking to a subsidiary company and for the reduction in the capital of the transferor-company. The Court ruled that the word arrangement is not specifically defined under the Act. It has a wide range and ambit. It includes restructuring of capital, reduction of capital and demerger. The scheme of arrangement having the ingredients of de-merger and reduction of share capital and scheme of arrangements with the concerned companies and trust cannot be said to be beyond the purview of sections of the Companies Act.

Answer to Question No. 2(b)

Buy Back through Book Building Route

A company can buy back its securities through the book building process as provided under Securities and Exchange Board of India (Buy Back of Securities) Regulations, 1998 which is as under:

1. (a) The special resolution as in Regulation 5 or 5A, should specify the maximum price at which the buy back will be made.

(b) The company should appoint a merchant banker.

(c) A public announcement as referred to in Regulation 8 shall be made atleast 7 days prior to the commencement of the buy back.

(d) Subject to the provisions of Sub- clauses (i) and (ii), the provisions of Regulation 10 regarding escrow account are applicable –

   (i) The deposit in the escrow account should be made before the date of the public announcement.

   (ii) The amount to be deposited in the escrow account should be determined with reference to the maximum price as specified in the public announcement.

(e) A copy of the public announcement must be filed with SEBI within two days of the announcement along with the fees specified in Schedule IV to the Regulations. The public announcement shall also contain the detailed methodology of the book building process, manner of acceptance, format
of acceptance to be sent by the security holders pursuant to public announcement and details of bidding centers.

(f) The book building process should be made through an electronically linked transparent facility.

(g) The number of bidding centers should not be less than thirty and there should be at least one electronically linked computer terminal at all the bidding centers.

(h) The offer for buy back should be kept open to the security holders for a period of not less than fifteen days and not exceeding thirty days.

(i) The merchant banker and the company should determine the buy back price based on the acceptances received and the final buy back price which should be the highest price accepted should be paid to all the holders whose securities have been accepted for the buy back.

(2) The provisions of Regulation 9(5) pertaining to verification of acceptances and the provisions of Regulation 11 pertaining to opening of special account and payment of consideration are applicable mutatis mutandis.

Question No. 3

(a) Reduction of capital is one of the modes of re-organisation of capital structure of the company and to a certain extent it can be done without the sanction of the court. Explain with relevant provisions of the law.

(b) In a scheme of compromise, arrangement, reconstruction or amalgamation, various types of approvals are required. Describe briefly such approvals.

(6 marks each)

Answer to Question No. 3(a)

A company may reorganize its capital in different ways which may include: (a) reduction of paid-up capital; (b) conversion of one type of shares into another; (c) conversion of shares into debentures. There may be many other ways and manner of reorganization of capital. Re-organization of share capital may be proposed between the company and its creditors or class of creditors or members or class of members and requires confirmation of CLB under Section 391. Reduction of capital means reduction of issued, subscribed and paid up capital of the company. Section 100 provides for the reduction of share capital, if the articles of the company so authorize with the confirmation of the Court.

However in following cases, reduction of share capital can be made without sanction of court.

(a) Surrender of Shares

This means the surrender of shares already issued to the company by the registered holder of shares. Where shares are surrendered to the company, whether by way of settlement of a dispute or for any other reason, it will have the same effect as a transfer in favour of the company and amount to reduction of capital. But if, under any arrangement such shares instead of being surrendered
to the company, are transferred to a nominee of the company then there will be no reduction of capital [Collector of Moradabad v. Equity Insurance Company Limited (1948) 18 Com Cases 309: AIR 1948 Oudh 197]. Surrender may be accepted by the company under the same circumstances where forfeiture is justified. It has the effect of releasing the shareholder whose surrender is accepted for further liability on shares.

The Companies Act contains no provisions for surrender of shares. Thus surrender of shares is valid only when Articles of Association provide for the same and:

(i) Where forfeiture of such shares is justified; or
(ii) When shares are surrended in exchange for new shares of same nominal value.

Both forfeiture and surrender lead to termination of membership. However, in the case of forfeiture it is at the initiative of the company and in the case of surrender it is at the initiative of member or shareholder.

(b) **Forfeiture of Shares**

A company may if authorized by its articles, forfeit shares for non-payment of calls and the same will not require confirmation of the court.

Where the power is given in the articles, it must be exercised strictly in accordance with the regulations regarding notice, procedure and manner stated therein, otherwise the forfeiture will be void. Forfeiture will be effected by means of Board resolution.

The power of forfeiture must be exercised bona fide and in the interest of the company.

(c) **Diminution of Capital**

Where the company cancels shares which have not been taken or agreed to be taken by any person. [Section 94(1)(3)].

(d) Redemption of redeemable preference shares.

(e) Purchase of shares of a member by the company under Section 402.

(f) Buy back of its own shares under Section 77A.

(g) Reduction of capital when company is defunct.

**Answer to Question No. 3(b)**

In a scheme of compromise or arrangement, following types of approvals are required to be obtained by the transferor and transferee companies:

(i) **Approval of the Boards of each of the Companies**: This is the first step to carry out amalgamation. Approval authorizes the director/company secretary to do everything for this purpose.

(ii) **Approval of Shareholders/Creditors**: This approval is to be obtained at specially convened meetings as per Court’s directions under Section 391(1) of the Companies Act. However, if all members consent in writing, this can be dispensed with. The unsecured / sundry creditors meetings are dispensed with subject to certain conditions.
(iii) **Approval of Stock Exchange**: In case of companies listed with recognized stock exchange(s), a no-objection certificate under Clause 24(f) of the listing agreement is to be obtained at least one month prior to filing it with High Court.

(iv) **Approval from Financial Institutions/Lending Banks/Debenture trustees etc.**: If the company has borrowed funds from the above lenders, approval is necessary from the lender and debenture trustees.

(v) **Approval from the land holders**: If the land on which the factory is situated is the lease-hold land and the terms of the lease deed so specifies, the approval from the lessor will be needed.

(vi) **Approval from Reserve Bank of India**: If amalgamation results to issuance of shares/cash option to the non-resident Indians, the amalgamated company has to obtain permission from Reserve Bank of India under Foreign Exchange Management (Transfer or issue of security by a person Resident outside India) Regulations, 2000.

(vii) **Approval of Competition Commission of India under Competition Act**: Under the Competition Act, regulation of combinations as provided under Sections 5 and 6 of the Act would also be required to be complied by companies, if applicable. Under the Competition Act, 2002, reference must be made to the Competition Commission of India in certain cases depending upon the post-merger size of the assets or business.

(viii) **Sanction of the respective High Courts**: Both amalgamated/resulting companies and amalgamating companies are required to seek approval from the respective High Court(s) in which their registered offices are situated.

**Question No. 4**

(a) The court has fixed meeting of equity shareholders of ABC Ltd. On Tuesday, the 12th August, 2013 at Asoka Hotel, New Delhi for considering the proposed scheme of amalgamation with XYZ Ltd. and appointed Mr. Joseph as Chairman and Mrs. Dyana as alternate Chairperson of the meeting. As a Company Secretary of ABC Ltd., draft the notice of the meeting.

(b) On meeting of equity shareholders of ABC Ltd., the proposed scheme of amalgamation of ABC Ltd. with XYZ Ltd. was passed. Draft the Chairman’s report for onward submission to the court.

**Answer to Question No. 4(a)**

**Form No. 36**

IN THE HIGH COURT OF JUDICATURE AT _____________

(ORIGINAL JURISDICTION)

In the matter of Companies Act, 1956

And

In the matter of Scheme of Amalgamation of ABC Ltd. with XYZ Ltd. ABC Ltd., an existing company under Companies Act, 1956 and having its registered office at ____________

Company Application No. __________ of 2013

ABC Ltd., Applicant
Notice Convening Meeting

To

Equity Shareholders

TAKE NOTICE that by an order made on ___________ day of ___________ 2013, the Court has directed that a meeting of the equity shareholders of the company be held at Asoka Hotel, New Delhi on 12th August, 2013 at _____AM/PM, for the purpose of considering and, if thought fit, approving with or without modification, the Scheme of Amalgamation proposed to be made between the Applicant Company and XYZ Ltd.

TAKE FURTHER NOTICE that in pursuance of the said order, a meeting of the equity shareholders of the Applicant Company will be held at Asoka Hotel, New Delhi on 12th August, 2013 at ____AM/PM which you are requested to attend.

TAKE FURTHER NOTICE that you may attend and vote at the said meeting in person or by proxy, provided that a proxy in the prescribed form, duly signed by you, is deposited at the registered office of the company at ___________ not later than 48 hours before the meeting. The quorum of the meeting shall be five members present in person or by proxy.

The Court has appointed Mr. Joseph as Chairman of the said meeting and Mrs. Dyana as alternate Chairperson of the meeting.

A copy of each of the Scheme of Amalgamation, the statement under Section 393 of the Companies Act, 1956 and a form of proxy and attendance slip are enclosed.

Dated this ___________ day of 2013

Sd/-
For ABC Ltd.

Mr. VBD
Company Secretary

Note: All alterations made in the form of Proxy should be initialed.

Answer to Question No. 4(b)

Form No. 39

IN THE HIGH COURT OF JUDICATURE AT ___________
(ORIGINAL JURISDICTION)
In the matter of Companies Act, 1956

And

In the matter of scheme of Amalgamation of ABC Ltd. with XYZ Ltd.
ABC Ltd., an existing company under Companies Act, 1956 and having its registered office at ___________

Company Application No. ___________ of 2013

ABC Ltd., Applicant
Report by Chairman

I, Mr. Joseph, Advocate, the person appointed by this Hon’ble Court to act as Chairman of the meeting of the equity shareholders of the above named company, summoned by notice served individually upon them and by advertisement dated the……..day of………. 201…….., and held on the 12th August, 2013 at Asoka Hotel, New Delhi, do hereby report to this Hon’ble Court as follows :

1. The said meeting was attended by…………………………equity shareholders personally holding……………..value of shares and ………….equity shareholders holding…………. value of shares have attended the said meeting through proxy.

2. The scheme of amalgamation was read out and explained by me to the meeting and questions raised were answered satisfactorily. The equity shareholders of the said company have approved the scheme of amalgamation submitted to the meeting and agreed thereto.

3. The said meeting was unanimously of the opinion that the scheme of amalgamation should be approved and agreed to/or. The result of the voting of the meeting are attached as per annexure A showing names and addresses of the equity shareholders, value of equity shares held by them, number of votes, approved or disapproved.

Dated this__________ day of 2013

Sd/-

Mr. Joseph
Chairman appointed for the meeting

Part B (30 Marks)

Question No. 5

Discuss briefly the meaning, objectives and scope of Valuation.     (8 marks)

Answer to Question No. 5

Valuation is an exercise to assess the worth of an enterprise or a property. In a merger or amalgamation or demerger or acquisition, valuation is certainly needed. It is essential to fix the value of the shares to be exchanged in a merger or the consideration payable for an acquisition.

The main objective in carrying out a valuation is to conclude a transaction in a reasonable manner without any room for any doubt or controversy about the value obtained by any party to the transaction.

The following are some of the usual circumstances when valuation of shares or enterprise becomes essential:

— When issuing shares to public either through an initial public offer or by offer for sale of shares of promoters or for further issue of shares to public.
— When promoters want to invite strategic investors or for pricing a first issue or a further issue, whether a preferential allotment or rights issue.

— In making investment in a joint venture by subscription or acquisition of shares or other securities convertible into shares.

— For making an ‘open offer for acquisition of shares’.

— When company intends to introduce a ‘buy back’ or ‘delisting of share’.

— If the scheme of merger or demerger involve issue of shares. In Schemes involving Mergers/Demergers, share valuation is resorted to in order to determine the consideration for the purpose of issue of shares or any other consideration to shareholders of transferor or demerged companies.

— On Directions of Company Law Board or any other Tribunal or Authority or Arbitration Tribunals directs.

— For determining fair price for effecting sale or transfer of shares as per Articles of Association of the Company.

— As required by the agreements between two parties.

— For purposes of arriving of Value of Shares for purposes of assessments under the Wealth Tax Act.

— To determine purchase price of a ‘block of shares’, which may or may not give the holder thereof a controlling interest in the company.

— To value the interest of dissenting shareholders under a scheme of Amalgamation merger or reconstruction.

— Conversion of Debt Instruments into Shares.

— Advancing a loan against the security of shares of the company by the Bank/Financial Institution.

— As required by provisions of law such the Companies Act, 1956 or Foreign Exchange Management Act, 1999 or Income Tax Act, 1961 or the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 [the Takeover Code] or SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 or SEBI (Buy Back of Securities) Regulations, 1998 or Delisting Guidelines.

**Question No. 6**

*Elucidate the principles involved in valuation.*  
(7 marks)

**Answer to Question No. 6**

Principles involved in valuation are as under:

— Value is determined at a specific point in time.

— Value is prospective. It is equivalent to the present value, or economic worth, of all future benefits anticipated to accrue from ownership.
— The market determines the required rate of return.
— Value is influenced by liquidity.
— The higher the underlying net tangible asset value base, the higher the going concern value.

Question No. 7

*Discuss about Market Based Valuation.*

**Answer to Question No. 7**

Market based valuation help the strategic buyer estimate the subject business value by comparison to similar businesses. Where the company is listed market price method that helps in evaluating on the price on the secondary market. Average of quoted price is considered as indicative of the value perception of the company by investors operating under free market conditions. To avoid chances of speculative pressures, it is suggested to adopt the average quotations of sufficiently longer period. The valuer will have to consider the effect of issue of bonus shares or rights shares during the period chosen for average.

(i) Market Price Method is not relevant in the following cases:

- Valuation of a division of a company.
- Where the share are not listed or are thinly traded.
- In the case of a merger, where the shares of one of the companies under consideration are not listed on any stock exchange.
- In case of companies, where there is an intention to liquidate it and to realise the assets and distribute the net proceeds.

(ii) In case of significant and unusual fluctuations in market price the market price may not be indicative of the true value of the share. At times, the valuer may also want to ignore this value, if according to the valuer, the market price is not a fair reflection of the company’s underlying assets or profitability status. The Market Price Method may also be used as a back up for supporting the value arrived at by using the other methods.

(iii) It is important to note that Regulatory bodies have often considered market value as one of the very important basis — Preferential allotment, Buyback, Open offer price calculation under the Takeover Code.

(iv) In earlier days due to non-availability of data, while calculating the value under the market price method, high and low of monthly share prices where considered. Now with the support of technology, detailed data is available for stock prices. It is now a usual practice to consider weighted average market price considering volume and value of each transaction reported at the stock exchange.

(v) If the period for which prices are considered also has impact on account of Bonus shares, Rights Issue, etc., the valuer needs to adjust the market prices for such corporate events.
Question No. 8

Critically examined the strategy involved in valuation of Securities. (8 marks)

Answer to Question No. 8

The following Strategies are involved in valuation of Securities:

— Background Information
— Purpose of Valuation and Appointing Authority
— Identity of the valuer and any other experts involved in the valuation
— Disclosure of valuer Interest/Conflict, if any
— Date of Appointment, Valuation Date and Date of Report
— Sources of Information
— Procedures adopted in carrying out the Valuation
— Valuation Methodology
— Major Factors influencing the Valuation
— Conclusion
— Caveats, Limitations and Disclaimers.

Part C (20 Marks)

Question No. 9

(a) Explain the enforcement of security interest by a secured creditor under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

(b) Define ‘Securitisation’ and explain the objectives of Securitisation. (5 marks each)

Answer to Question No. 9(a)

Under Section 13 of the Securitization and Reconstruction of Financial assets and Enforcement of Security Interest Act, 2002(hereinafter Securitization Act), secured creditor can enforce his security interest without intervention of the Court, on default in repayment of instalments, and non compliance with the notice of 60 days after the declaration of the loan as a non-performing asset. In case of the default in repayment of installment by the borrower and debts becoming NPA, the secured creditor has two options. It can either transfer the assets to a securitisation or reconstruction company or exercise the powers under the Act.

Section 13(4) of the Act empowers the recourse to one more of the following measures, after giving proper notice, for the recovery of the secured debts, namely:

— Take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset;
— Take over the management of the secured assets of the borrower including the
right to transfer by way of lease, assignment or sale and realize the secured asset;

— Appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;

— Require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

**Answer to Question No. 9(b)**

According to Section 2(1)(z) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, “Securitisation” means acquisition of financial assets by any securitisation company or reconstruction company from any originator, whether by raising of funds by such securitisation company or reconstruction company from qualified institutional buyers by issue of security receipts representing undivided interest in such financial assets or otherwise.

There are two motives for Securitisation. One, the securitised assets go off the balance sheet of the originator and so the asset base is pruned down to that extent, thereby reducing the regulatory capital requirements to support the assets. Second, the asset portfolio is liquidated; releasing cash, which in turn reduces the need for demand and time liabilities that are subject to statutory reserves.

**Question No. 10**

(a) **What do you mean by ‘non-performing assets’ under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002?**

(b) **What do you understand by ‘sick industrial company’? Explain the immunities provided to a sick industrial company under the Sick Industrial Companies (Special Provisions) Act, 1985.** (5 marks each)

**Answer to Question No. 10(a)**

According to Section 2(1)(o) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 “Non-Performing Asset” means an asset or account of a borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset—

(a) in case such bank or financial institution is administered or regulated by an authority or body established, constituted or appointed by any law for the time being in force, in accordance with the directions or guidelines relating to assets classifications issued by such authority or body;

(b) in any other case, in accordance with the directions or guidelines relating to assets classifications issued by the Reserve Bank.

In *Srinivas Rice & Floor Mill v. Authorized Officer, State Bank of India*, [2008] 81 SCL 66 (AP), the AP High Court held that there is no statutory format, express or by necessary implication, that require the Banks to follow a particular or formal procedure
or require a formal declaration as a condition precedent to classification of debt as “NPA”. What section 13(2) r/w Section 2(1)(o) requires is a classification of a debt by a bank as ‘NPA’ within the legislative guidelines spelt out in the definition of NPA.

**Answer to Question No. 10(b)**

According to Section 3(1)(o) of the Sick Industrial Companies (Special Provisions) Act, 1985, “sick industrial company” means an industrial company (being a company registered for not less than five years), which has at the end of any financial year accumulated losses equal to or exceeding its entire net worth.

*Explanation*: For the removal of doubts, it is hereby declared that an industrial company existing immediately before the commencement of the Sick Industrial Companies (Special Provisions) Amendment Act, 1993 registered for not less than five years and having at the end of any financial year accumulated losses equal to or exceeding its entire net worth, shall be deemed to be a sick industrial company.

Immunities to a sick industrial company has been granted under the provisions of Section 22 of the SICA, 1985. This Section provides that in certain circumstances, no proceedings for the winding up of the industrial company or for execution, distress or the like against any of the properties of the industrial company or for the appointment of a receiver in respect thereof and no suit for the recovery money or for the enforcement of any security against the industrial company or of any guarantee in respect of any loans or advance granted to the industrial company shall lie or be proceeded with further, except with the consent of BIFR or, as the case may be, the Appellate Authority.

The protection under Section 22 of SICA is available in respect of an industrial company when an inquiry under Section 16 is pending in relation to the said industrial company or when any scheme referred to under Section 17 is under preparation or consideration or a sanctioned scheme is under implementation or where an appeal under Section 25 relating to an industrial company is pending.

BIFR may by order declare with respect to the sick industrial company concerned that the operation of all or any of the contracts, assurances of property, agreements, settlements, awards, standing orders or other instruments in force, applicable to the sick industrial company in question shall remain suspended or that all or any of the rights, privileges, obligations, and liabilities accruing or arising thereunder before the said date, shall remain suspended or shall be enforceable with such adaptations and in such manner as may be specified by BIFR. Provided that such declaration shall not be made for a period exceeding two years which may be extended by one year at a time so, however, that the total period shall not exceed seven years in the aggregate. Any such declaration is valid and is protected notwithstanding anything contained in the Companies Act, 1956, or any other law or agreement or instrument or any decree or order of a court, Tribunal, officer or other authority or of any submission, settlement or standing order.

Section 22 does not grant immunity against the criminal proceedings against the company or its directors.
Question No. 1

(a) “Section 391 is a boon to the corporate restructuring.” Critically examine the statement and discuss the relevant provisions relating to corporate restructuring.

(b) Will the Court sanction a scheme of amalgamation where companies to the scheme tend to reshuffle their objects clause in the memorandum of association? Support your answer with case law.

(5 marks each)

Answer to Question No. 1(a)

Section 391 of the Companies Act, 1956 is a boon to corporate restructuring. This section along with Section 394, has proved to be a major legislative blessing for corporate restructuring in a variety of ways, such as amalgamation (merger) of two or more companies, demerger, division or partition of a company into two or more companies, hiving off a unit, as well as a compromise with the members or creditors of a company or an arrangement with respect to the share capital, assets or liabilities of the company etc.

It has been held in several cases that Section 391 is a ‘complete code’ or ‘single window clearance system’, and that the Court has been given wide powers under this section, to frame a scheme for the revival of a company. Being a complete code, the Court can, under this ‘section’, sanction a scheme containing all the alterations required in the structure of the company for the purpose of carrying out of the scheme.

Section 391 contemplates a compromise or arrangement between a company and its creditors or any class of them, or its members or any class of them, and provides machinery whereby such a compromise or arrangement may be binding on dissentient persons by an order of the Court. [Oceanic Steam Navigation Co. In re. (1939) 9 Comp. Cas. 229 (Ch.D)].

Answer to Question No. 1(b)

Court will sanction the scheme if alteration of the memorandum is by reshuffling of the Objects Clause by shifting Other Objects to Main Objects, if transferee company has complied with provisions of Section 149(2A) of Companies Act, 1956. [Re: Rangkala Investments Ltd. (1996) 1 Comp LJ 298 (Guj)].

Question No. 2

(a) Enumerate the factors that the Competition Commission of India have due regard while determining whether a combination would have appreciable adverse effect on competition.
(b) Briefly explain with relevant provisions of the Companies Act, 1956 as to when the scheme of amalgamation would become effective. (5 marks each)

**Answer to Question No. 2(a)**

The Commission under Section 20 of the Competition Act, 2002 shall have due regard to all or any of the factors for the purposes of determining whether the combination would have the effect of or is likely to have an appreciable adverse effect on competition in the relevant market, namely:

(a) actual and potential level of competition through imports in the market;
(b) extent of barriers to entry into the market;
(c) level of combination in the market;
(d) degree of countervailing power in the market;
(e) likelihood that the combination would result in the parties to the combination being able to significantly and sustainably increase prices or profit margins;
(f) extent of effective competition likely to sustain in a market;
(g) extent to which substitutes are available or likely to be available in the market;
(h) market share, in the relevant market, of the persons or enterprise in a combination, individually and as a combination;
(i) likelihood that the combination would result in the removal of a vigorous and effective competitor or competitors in the market;
(j) nature and extent of vertical integration in the market;
(k) possibility of a failing business;
(l) nature and extent of innovation;
(m) relative advantage, by way of the contribution to the economic development, by any combination having or likely to have appreciable adverse effect on competition;
(n) whether the benefits of the combination outweigh the adverse impact of the combination, if any.

**Answer to Question No. 2(b)**

According to the provisions of Section 391(3) and 394(3) of the Companies Act, 1956, certified copy of the order passed by the Court shall be filed with the concerned Registrar of Companies. This is required to be filed with e-form 21 which is required to be filed within thirty days of the making of the order. Date of completion of the last of the required approvals shall be treated as effective date for the scheme of amalgamation.

**Question No. 3**

(a) _Whether in a scheme of arrangement the meeting of shareholders and creditors can be dispensed with?_ Supplement your answer with the help of case law.
(b) Though the terms ‘diminution of share capital’ and ‘reduction of capital’ look synonymous, but sometimes diminution of share capital does not amount to reduction of capital. Briefly explain the circumstances when such exercises do not fall within the purview of ‘reduction of capital’ and procedure of reduction of capital under section 100 is not to be followed. (5 marks each)

Answer to Question No. 3(a)

Members’ and creditors’ approval to the scheme of amalgamation is sine qua non for Court’s sanction. Without that the Court cannot proceed. This approval is to be obtained at specially convened meetings held as per court’s directions [Section 391(1) of the Companies Act, 1956]. However, the court may dispense with meetings of members/creditors. Normally, creditors’ meetings are dispensed with subject to certain conditions. For instance, members’ meeting may be dispensed with if all the members’ individual consent is obtained.

Where the written consent to the proposed scheme is granted by all the members and secured and unsecured creditors, separate meeting of members and secured and unsecured creditors can be dispensed with. – [Re Feedback Reach Consultancy Services (P) Ltd. (2003) 52 CLA 260: (2003) CLC 498: (2003) 42 SCL 82: (2003) 115 Comp Cas 897 (Del)].

Answer to Question No. 3(b)

Though the terms ‘diminution of share capital’ and ‘reduction of capital’ look synonymous, but sometimes diminution of share capital does not amount to reduction of capital. In the following cases, the diminution of share capital is not to be treated as reduction of the capital:

(i) Where the company cancels shares which have not been taken or agreed to be taken by any person [Section 94(1)(e)];

(ii) Where redeemable preference shares are redeemed in accordance with the provisions of Section 80;

(iii) Where the company buys-back its own shares under Section 77A of the Act.

In the above mentioned situations, the procedure for reduction of capital as laid down in Section 100 of the Companies Act, 1956 is not attracted.

Question No. 4

Draft a suitable Board resolution with respect to takeover for the following:

(i) Appointment of a merchant banker,

(ii) Opening of an Escrow account. (5 marks each)

Answer to Question No. 4(i)

Appointment of Merchant Banker

“RESOLVED THAT M/s …………… being Category-I Merchant Banker be and is hereby appointed as Merchant Banker for aforesaid public offer, on the terms and conditions as contained in the draft letter of appointment placed before the meeting duly
initialed by the Chairman for the purpose of identification, for making the public announcement of the takeover offer in the newspapers, forward the same to the Securities and Exchange Board of India, Stock Exchange(s) and to the target company and to draft the Letter of Offer to be sent to the shareholders of ………, target company in accordance with the SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011”.

Answer to Question No. 4(ii)

Opening of Escrow Account

“RESOLVED THAT an Escrow Account be opened with ………………. Bank and Rs. ……………..be deposited in the said account.

RESOLVED FURTHER THAT M/s……………, Merchant Banker, be and is hereby authorised to operate the above said account and the Bank be and is hereby authorised to act on the instructions given by M/s ……………., Merchant Banker, in relation to operation of bank account.”

RESOLVED FURTHER THAT Mr. ………, Director of the company, be and is hereby authorised to collect and communicate the same to…………….Bank, the names and specimen signatures of the person authorised by M/s. ……….., Merchant Banker, to operate the above said bank account.”

Question No. 5

(a) Define ‘corporate restructuring’. What are the various kinds of restructuring?

(b) ABC Ltd. proposes to amalgamate with BCD Ltd. In this context, explain how to go about for convening the meeting of the creditors or class of creditors in terms of court’s order. (5 marks each)

Answer to Question No. 5(a)

The meaning of the term ‘Corporate Restructuring’ is quite wide and varied. Depending upon the requirements of a company, it is possible to restructure its business, financial and organizational transactions in different forms. Restructuring is a method of changing the organizational structure in order to achieve the strategic goals of the organization or to sharpen the focus on achieving them. The essentials of Corporate Restructuring are efficient and competitive business operations by increasing the market share, brand power and synergies. Simply stating, the expression ‘Corporate Restructuring’ implies restructuring or reorganizing a company or its business (or one of its businesses) or its financial structure, in such a way as to make it operate more effectively.

Restructuring may be of the following kinds:

Financial restructuring which deals with the restructuring of capital base and raising finance for new projects. This involves decisions relating to acquisitions, mergers, joint ventures and strategic alliances.

Technological restructuring which involves, inter alia, alliances with other companies to exploit technological expertise.

Market restructuring which involves decisions with respect to the product market segments, where the company plans to operate based on its core competencies.
Organizational restructuring which involves establishing internal structures and procedures for improving the capability of the personnel in the organization to respond to changes.

**Answer to Question No. 5(b)**

After receiving the court’s order for convening the meeting of creditors or class of creditors as per section 391(1) of the Companies Act, 1956, the meetings are to be held as per directions of the Court under the chairmanship of the person appointed by the Court for the purpose. Normally, the Court appoints a Chairman and alternate Chairman of each meeting. The procedural aspects for convening the meeting of the creditors or class of creditors in terms of court’s orders are as follows –

1. The notice and explanatory statement under Section 393 of the Companies Act, 1956 with the form of proxy and specimen advertisement in the newspapers as approved by the Court alone should be issued.
2. Notice shall be issued to all the creditors of the Company or a class of creditors as directed by the Court.
3. The advertisement of the meeting shall be given in the approved format in newspapers approved by the Court.
4. Keep the venue of the meeting ready for the event.
5. Usually the Court may appoint a chairman for the meeting. Otherwise the Court approves the chairman or any other named director to chair the meetings.
6. The quorum shall be as specified in the direction of the Court.
7. As per Companies Court rules, 1959, even the presence of a proxy is counted for quorum purposes.
8. The meeting shall commence at the appointed time.
9. A copy of the scheme; particulars of creditors, class-wise, copies of notices and other records, financial statements, value of debt due to a creditor should be kept ready.
10. Proper arrangements should be made for voting.
11. When a resolution is put to vote, proper count shall be taken of those who are present and voting.
12. Chairman shall ask the scrutinizer to submit a report on the result of voting and the value thereof.
13. Chairman shall prepare the minutes of the meeting and furnish a report to the Court.

**Part B (30 Marks)**

**Question No. 6**

*Write short notes on the following:*

(i) **Valuation Standard**
Answer to Question No. 6(i)

Valuation Standards aims to provide uniformity in valuation of various tangible and intangible classes of assets that provides consistent delivery of standards.

The International Valuation Standards Council is the established international standard setter for valuation. Through the International Valuation Standards Board, the IVSC develops and maintains standards on how to undertake and report valuations, especially those that will be relied upon by investors and other third party stakeholders. The IVSC also supports the need to develop a framework of guidance on best practice for valuations of the various classes of assets and liabilities and for the consistent delivery of the standards by properly trained professionals around the globe.

The IVSC has published International Valuation Standards (IVS) since 1985. Membership of IVSC is open to organisations of users, providers, professional institutes, educators, and regulators of valuation services. IVSC members appoint the IVSC Board of Trustees.

Answer to Question No. 6(ii)

Documentation is “an essential element” of Valuation quality. Valuation documentation provides the principal written record to support the following:

- The Valuer’s report assertion that the valuation exercise was performed with due diligence and in accordance of generally accepted valuation principles and
- The Valuers’ conclusions about Valuation of the subject matter of the Valuation exercise and other related aspects of valuation.

Valuation documentation must clearly demonstrate that the Valuation exercise was in fact performed in compliance with generally accepted valuation principles and applicable standards. It must provide a clear link to valuation conclusions and must contain sufficient information, in sufficient detail, for a clear understanding of the following:

- The nature, timing, and extent of the valuation exercise;
- The work performed;
- The purpose of the valuation;
- The source of the information analyzed and supporting evidential matter obtained, examined, and evaluated; and
- The conclusions reached.

Answer to Question No. 6(iii)

Black’s Dictionary defines brand as a word, mark, symbol, design, term, or a combination of these, both visual and oral, used for the purpose of identification of some product or service. It is the hallmark of a shrewd businessman to commence his business with a roadmap of his plans. In the course of his business, he applies a unique mark or symbol or word to his goods. When his customer base increases, his goods acquire
reasonable reputation and his customers begin identifying his goods by the unique mark or symbol or word he had so adopted, his goods earn the reputation of being branded goods. What applies to goods applies to services also. When brands take charge of consumers’ minds, the name of its proprietor takes the backseat. There lies the power of brands.

Think for a moment as to how much investment one has to make by means of money and others resources to adopt, develop and popularize a brand or a mark during the course of his business. Brands/marks are a class of assets like human resource, knowledge etc. They create a value premium for the goods and services. Therefore, without the brand/mark, the goods/services may be address less. In order to market it or use this asset wisely valuing the same is essential. But remember, valuing a brand is a very difficult task. There is no prescribed manner to value a brand. But all knows that brands connect markets with products and thereby they create value.

Brands do not command any value unless they are able bring cash flows to the Company that has adopted the same. With incremental cash flows increasing, value of brand increases proportionately. Brands have to be constantly associated with good quality goods and services; they require proper show casing and servicing and they should remain active in appropriate markets.

Question No. 7

Discuss about preliminary work relating to valuation. (8 marks)

Answer to Question No. 7

Preliminary Steps in Valuation

A business/corporate valuation involves analytical and logical application/analysis of historical/future tangible and intangible attributes of business. The preliminary study to valuation involves the following aspects:

1. Analysis of Business History
2. Profit trends
3. Goodwill/Brand name in the market
4. Identifying economic factors directly affecting business
5. Study of Exchange risk involved
6. Study of Employee morale
7. Study of market capitalization aspects
8. Identification of hidden liabilities through analysis of material contracts.

Question No. 8

Explain the regulatory aspect of valuation under SEBI (ICDR) Regulations. (7 marks)

Answer to Question No. 8

Pricing

(1) An issuer may determine the price of specified securities in consultation with the lead merchant banker or through the book building process.
(2) An issuer may determine the coupon rate and conversion price of convertible debt instruments in consultation with the lead merchant banker or through the book building process.

**Differential pricing**

An issuer may offer specified securities at different prices, subject to the following:

(a) retail individual investors or retail individual shareholders or employees of the issuer entitled for reservation made under regulation 42 making an application for specified securities of value not more than one lakh rupees, may be offered specified securities at a price lower than the price at which net offer is made to other categories of applicants:

Provided that such difference shall not be more than ten per cent of the price at which specified securities are offered to other categories of applicant;

(b) in case of a book built issue, the price of the specified securities offered to an anchor investor shall not be lower than the price offered to other applicants;

(c) in case of a composite issue, the price of the specified securities offered in the public issue may be different from the price offered in rights issue and justification for such price difference shall be given in the offer document.

**Price and price band**

(1) The issuer may mention a price or price band in the draft prospectus (in case of a fixed price issue) and floorrice or price band in the red herring prospectus (in case of a book built issue) and determine the price at a later date before registering the prospectus with the Registrar of Companies:

Provided that the prospectus registered with the Registrar of Companies shall contain only one price or the specified coupon rate, as the case may be.

(2) If the floor price or price band is not mentioned in the red herring prospectus, the issuer shall announce the floor price or price band at least two working days before the opening of the bid (in case of an initial public offer) and at least one working day before the opening of the bid (in case of a further public offer), in all the newspapers in which the pre issue advertisement was released.

(3) The announcement shall contain relevant financial ratios computed for both upper and lower end of the price band and also a statement drawing attention of the investors to the section titled “basis of issue price” in the prospectus.

(4) The cap on the price band shall be less than equal to one hundred and twenty per cent of the floor price.

(5) The floor price or the final price shall not be less than the face value of the specified securities.

It may be noted that the “cap on the price band” includes cap on the coupon rate in case of convertible debt instruments.

**Face value of equity shares**

(1) Subject to the provisions of the Companies Act, 1956 and the ICDR
(Regulations), an issuer making an initial public offer may determine the face value of equity shares in the following manner:

(a) if the issue price per equity share is five hundred rupees or more, the issuer shall have the option to determine the face value at less than ten rupees per equity share;

Provided that the face value shall not be less than one rupee per equity share;

(b) if the issuer price per equity share is less than five hundred rupees, the face value of the equity shares shall be ten rupees per equity share:

The above mention criteria shall not apply to initial public offer made by any government company, statutory authority or corporation or any special purpose vehicle set up by any of them, which is engaged in infrastructure sector.

(2) The disclosure about the face value of equity shares (including the statement about the issue price being “X” times of the face value) shall be made in the advertisements, offer documents and application forms in identical font size as that of issue price or price band.

(a) If listed for more than 6 months

If the equity shares of the issuer have been listed on a recognised stock exchange for a period of six months or more as on the relevant date, the equity shares shall be allotted at a price not less than higher of the following:

(i) The average of the weekly high and low of the closing prices of the related equity shares quoted on the recognised stock exchange during the six months preceding the relevant date; or

(ii) The average of the weekly high and low of the closing prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.

(b) If listed for less than 6 months

If the equity shares of the issuer have been listed on a recognised stock exchange for a period of less than six months as on the relevant date, the equity shares shall be allotted at a price not less than the higher of the following:

(i) the price at which equity shares were issued by the issuer in its initial public offer or the value per share arrived at in a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956, pursuant to which the equity shares of the issuer were listed, as the case may be; or

(ii) the average of the weekly high and low of the closing prices of the related equity shares quoted on the recognised stock exchange during the period shares have been listed preceding the relevant date; or

(c) the average of the weekly high and low of the closing prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.
This price shall be recomputed by the issuer on completion of six months from the date of listing on a recognised stock exchange with reference to the average of the weekly high and low of the closing prices of the related equity shares quoted on the recognised stock exchange during these six months and if such recomputed price is higher than the price paid on allotment, the difference shall be paid by the allottees to the issuer.

Part C (20 Marks)

Question No. 9

(a) State the World Bank principles for effective insolvency and creditor rights systems.

(b) ABC Bank Ltd. has approached you for your professional advice about the rights available to it for enforcing the security interest under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002. Highlight the rights and the advantages to the bank by resorting to that mode of recovery citing the relevant provisions of the said Act.

Answer to Question No. 9(a)

The World Bank Principles for effective insolvency and creditor rights system have been designed as a broad-spectrum assessment tool to assist countries in their efforts to evaluate and improve core aspects of their commercial law systems that are fundamental to a sound investment climate, and to promote commerce and economic growth.

The Principles emphasize contextual, integrated solutions and the policy choices involved in developing those solutions. The Principles highlight the relationship between the cost and flow of credit (including secured credit) and the laws and institutions that recognize and enforce credit agreements (Part A). The Principles also outline key features and policy choices relating to the legal framework for risk management and informal corporate workout systems (Part B), formal commercial insolvency law frameworks (Part C) and the implementation of these systems through sound institutional and regulatory frameworks (Part D).

The principles have broader application beyond corporate insolvency regimes and creditor rights. The Principles are designed to be flexible in their application, and do not offer detailed prescriptions for national systems. The Principles embrace practices that have been widely recognized and accepted as good practices internationally. As legal systems and business and commerce are evolutionary in nature, so too are the Principles, and it is anticipated that these will continue to be reviewed going forward to take account of significant changes and developments.

Answer to Question No. 9(b)

Enforcement of Security interest by Creditors

Section 13 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 provides for the enforcement of security
interest by a secured creditor straight away without intervention of the court, on default in repayment of instalments, and non compliance with the notice of 60 days after the declaration of the loan as a non-performing asset. It must, however, be remembered that the classification of assets as non performing is not on the mere whims and fancies of the financial institutions. The Reserve Bank of India has a detailed policy providing guidelines or prudential norms in that regard.

Section 13(4) of the Act empowers the recourse to one more of the following measures, after giving proper notice, for the recovery of the secured debts, namely:

— Take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset;
— Take over the management of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale and realize the secured asset;
— Appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;
— Require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

**Advantages**

(i) Bank can take possession of the security and sell it without the intervention of court.

(ii) As per section 15 of the Act –

(a) On publication of the notice of taking over the management of the business of the borrower the directors of the company or administrators of the business deemed to have vacated their office.

(b) Shareholders cannot pass resolutions or appoint directors without the consent of the bank.

(c) No proceeding for winding up of the borrower company or the appointment of receiver shall lie in any court without the consent of the bank.

(d) If any reference is pending, it shall abate if 75% of the secured creditors have taken measures to recover their secured debts.

**Question No. 10**

(a) **XYZ Bank Ltd. has obtained a decree from a civil court to recover an amount of Rs. 20 lakh with 12% interest and the court has allowed it to proceed against the commercial building given as security for the loan. Can the decree be treated as a debt under the SARFAESI Act, 2002? Cite the relevant provisions of law in support of your answer.**

(b) **Discuss the factors in which the court order winding up of the company under “just and equitable” ground.** (5 marks each)
Answer to Question No. 10(a)

As per Section 2(g) of the SARFAESI Act, “Debt” means any liability (inclusive of interest) which is claimed alleged as due from any person by a bank or a financial institution or by a consortium of banks or financial institutions during the course of any business activity undertaken by the bank or the financial institution or the consortium under any law for the time being in force, in cash or otherwise, whether secured or unsecured, or assigned or whether payable under a decree or order of any civil court or any arbitration award or otherwise or under a mortgagee and subsisting on, and legally recoverable on, the date of the application.

So, in accordance with the provision of Section 2(g) of SARFAESI Act, the decree obtained by XYZ Ltd. can be treated as a debt.

Answer to Question No. 10(b)

The Court ordered winding up of the company under ‘just and equitable’ clause to indicate the general categories:

— Where the whole object of the company was fraudulent [In Re. German Date Coffee Co., (1882) 20 Ch.D. 169].

— Where the substratum of the company is gone. The substratum of a company is deemed to have gone where (a) the subject matter of the company is gone, or (b) the object for which it was formed has substantially failed, or (c) it is impossible to carry on the business of the company except at a loss, or (d) the existing and possible assets are insufficient to meet the existing liabilities of the company (Seth Mohan Lal v. Grain Chambers Ltd., AIR 1968 S.C. 772).

— Where the main object of the company for which it was incorporated has been completely achieved.

— Where there is a complete deadlock in the management of the company e.g., where two shareholders, who were also directors of private company, were not on speaking term [In Re. Yenidjye Tobacco (1916) 2 Ch. 426]. Fractions among shareholders is, however, not a sufficient ground.

— Where the company is a “bubble” and has no business to carry on e.g. where the main business of the company has been taken over by the Government and there is no prospect of the company doing any other business mentioned in the objects clause of the Memorandum of Association.

— Where the company is insolvent and its business is being carried on for the benefit of the debenture holders.

— Where there has been mismanagement and misapplication of funds by the directors of private company [Lock v. John Blackwood Ltd., (1924) A.C. 73].

— Where the petitioner was excluded from all participation in the business of a private company.

— If the company has committed default in making payment to various investors, allegations that directors have cheated several thousand investors, banks and FIs, company has not filed balance sheet for two years and no reply from company to advertisement under Rule 24, the company is liable to be wound up [ROC v. Country Informtech Services P. Ltd. (2002) 39 SCL 504 (All HC)].
Question No. 1

(a) Explain the circumstances where reduction of share capital is done without confirmation by the court.

(b) Discuss the factors involved in Post Merger Reorganisation. (5 marks each)

Answer to Question No. 1(a)

The following are cases which amount to reduction of share capital but where no confirmation by the Court is necessary:

(a) Surrender of shares – Where shares are surrendered to the company, whether by way of settlement of a dispute or for any other reason, it will have the same effect as a transfer in favour of the company and amount to a reduction of capital.

(b) Forfeiture of shares – A company may if authorised by its articles, forfeit shares for non-payment of calls and the same will not require confirmation of the Court, when it is re-issued.

(c) Diminution of capital – Where the company cancels shares which have not been taken or agreed to be taken by any person [Section 94(1)(3)].

(d) Redemption of redeemable preference shares.

(e) Purchase of shares of a member by the company under Section 402.

(f) Buy-back of its own shares under Section 77A.

Answer to Question No. 1(b)

Factors involved in Post Merger Reorganisation are as under:

— Change of Name and Logo
— Revised Organization
— Communication
— Employee Compensation, Benefits and Welfare Activities
— Aligning Company Policies
— Aligning Accounting and Internal Database Management Systems
— Re-Visiting Internal Processes
— Re-Allocation of People
— Engagement with Statutory Authorities
— Record Keeping
— Immoveable Property
— Expansion of Existing Teams to Support Larger Organization
— Revised ISO Certification and Similar Other Certifications
— Re-Visiting Past Decisions/Government Approvals/Compliances
— Contracts

Question No. 2

(a) What is the difference between ‘compromise’ and ‘arrangement’?

(b) Explain briefly the procedure for making application to court under section 391 for directions to hold meetings of shareholders/creditors. (5 marks each)

Answer to Question No. 2(a)

Difference between Compromise and Arrangement

The meaning of the expression ‘arrangement’ as given under Section 390(b) of the Companies Act, 1956 includes reorganization of share capital of the company by consolidation of shares of different classes or division into different classes of shares or both. ‘Compromise’ presupposes the existence of a dispute which it seeks to settle. Nothing like that is implied in the ‘arrangement’ which has wider meaning than ‘compromise’. An arrangement involves an exchange of one set of rights and liabilities for another. All modes of reorganizing the share capital, takeover of shares of one company by another including interference with preferential and other special rights attached to shares can form part of an arrangement proposed with members.

Answer to Question No. 2(b)

Application to High Court seeking direction to hold meetings

Rule 67 of the Companies (Court) Rules, 1959 lays down that an application under Section 391(1) of the Companies Act, 1956 for an order seeking direction for convening meeting(s) of creditors and/or members or any class of them shall be by way of Judge’s summons supported by an affidavit. A copy of the proposed scheme should be annexed to the affidavit as an exhibit thereto. The summons should be moved ex parte in Form No. 33 of the Companies (Court) Rules, 1959. The affidavit in support of the application should be in Form No. 34.

Question No. 3

(a) State briefly the requirements for disclosure of pledged shares under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

(b) Explain the provisions relating to ‘escrow account’ under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011. (5 marks each)
**Answer to Question No. 3(a)**

As per Regulation 28(3) of the SEBI (SAST) Regulation, 2011, the term “encumbrance” shall include a pledge, lien or any such transaction, by whatever name called.

Regulation 31 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 deals with disclosure of encumbered shares. As per this Regulation

(1) The promoter of every target company shall disclose details of shares in such target company encumbered by him or by persons acting in concert with him in such form as may be specified.

(2) The promoter of every target company shall disclose details of any invocation of such encumbrance or release of such encumbrance of shares in such form as may be specified.

(3) The disclosures required under sub-regulation (1) and sub-regulation (2) shall be made within seven working days from the creation or invocation or release of encumbrance, as the case may be to,—
   (a) every stock exchange where the shares of the target company are listed; and
   (b) the target company at its registered office.

**Answer to Question No. 3(b)**

Regulation 17 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 deals with provisions of “escrow account”.

(1) Not later than two working days prior to the date of the detailed public statement of the open offer for acquiring shares, the acquirer shall create an escrow account towards security for performance of his obligations under these regulations, and deposit in escrow account such aggregate amount as per the following scale:

<table>
<thead>
<tr>
<th>Sl.No.</th>
<th>Consideration payable under the Open Offer</th>
<th>Escrow Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>On the first five hundred crore rupees</td>
<td>an amount equal to twenty-five per cent of the consideration</td>
</tr>
<tr>
<td>b</td>
<td>On the balance consideration</td>
<td>an additional amount equal to ten per cent of the balance consideration</td>
</tr>
</tbody>
</table>

Provided that where an open offer is made conditional upon minimum level of acceptance, hundred percent of the consideration payable in respect of minimum level of acceptance or fifty per cent of the consideration payable under the open offer, whichever is higher, shall be deposited in cash in the escrow account.

(2) The escrow account referred to in sub-regulation (1) may be in the form of,—
   (a) cash deposited with any scheduled commercial bank;
   (b) bank guarantee issued in favour of the manager to the open offer by any scheduled commercial bank; or
(c) deposit of frequently traded and freely transferable equity shares or other freely transferable securities with appropriate margin:

**Question No. 4**

Draft a suitable Board resolution with respect to takeover for the following:

(i) offer by offeror company; and
(ii) authorisation to invest in the shares of investee company. (5 marks each)

**Answer to Question No. 4(i)**

**Offer by Offeror Company**

RESOLVED THAT an offer be made, to the persons who are the members of ........... Ltd. as on............., for acquisition of............. equity shares of Rs. 10/- each representing a.............% of the total issued capital of the.....................Ltd.

RESOLVED FURTHER THAT above said offer shall remain open till............. at a price of Rs. .......... each.

RESOLVED FURTHER THAT shares be accepted even if such shares in aggregate are less than the limit mentioned above and in case shares offered exceed the limit, the company shall have an option to accept or reject the same in consultation with the concerned authorities and offer will be accepted according to the order in which they are received and full shareholding of the members accepting the offer be acquired subject to abovementioned limit."

**Answer to Question No. 4(ii)**

**Authorisation to invest in the shares of investee company**

Board Meeting Resolution under section 372A of the Companies Act, 1956. Resolved that pursuant to section 372A and other applicable provisions if any, of the Companies Act, 1956 and authorization given by the members of the company at their meeting held on ................. unanimous consent of the Board of Directors be and is hereby given to invest upto ........ equity shares of M/s. ABC Ltd. at a price of Rs........ each.

**Question No. 5**

(a) It is a well known fact that to maximise the shareholders value, a company having surplus funds often induced to buy-back its own shares. What are common reasons which usually induces a company to resort to buy-back?

(b) A listed company had drafted a special resolution to be passed through postal ballot to buyback 25% of its paid-up equity share capital. As a Company Secretary, you are required to draft the explanatory statement to the proposed resolution. What factors will you consider to prepare the explanatory statement? (5 marks each)

**Answer to Question No. 5(a)**

Good corporate governance calls for maximizing the shareholder value. When a company has surplus funds for which it does not have good avenues for deployment
assuring an average return on capital employed and earnings per share, the company’s financial structure requires balancing.

The reasons for buy-back may be one or more of the following:

- to improve earnings per share;
- to improve return on capital, return on net worth and to enhance the long-term shareholder value;
- to provide an additional exit route to shareholders when shares are under valued or are thinly traded;
- to enhance consolidation of stake in the company;
- to prevent unwelcome takeover bids;
- to return surplus cash to shareholders;
- to achieve optimum capital structure;
- to support share price during periods of sluggish market conditions;
- to service the equity more efficiently.

The decision to buy-back is also influenced by various other factors relating to the company, such as growth opportunities, capital structure, sourcing of funds, cost of capital and optimum allocation of funds generated.

Answer to Question No. 5(b)

Whereas unlisted companies should obtain shareholders’ approval by passing the special resolution only at a duly convened general meeting, listed companies should obtain such approval by postal ballot.

The notice containing the special resolution proposed to be passed should be accompanied by an explanatory statement stating:

- all material facts, fully and completely disclosed;
- the necessity for buy-back;
- the class of security intended to be purchased under the buy-back;
- the amount to be invested under buy-back; and
- the time limit for completion of buy-back.

Part B (30 Marks)

Question No. 6

Write short notes on the following:

(i) Asset Based Valuation
(ii) Valuation during Corporate Insolvency
(iii) Market Comparables. (5 marks each)
Answer to Question No. 6(i)

Asset Based Valuation

Asset based valuation method is based on the simple assumption that adding the value of all the assets of the company and subtracting the liabilities, leaving a net asset valuation, can best determine the value of a business. However, for the purposes of the amalgamation the amount of the consideration for the acquisition of a business may be arrived at either by valuing its individual assets and goodwill or by valuing the business as a whole by reference to its earning capacity.

This method may be summarized as: The procedure of arriving at the value of a share employed in the equity method is simply to estimate what the assets less liabilities are worth, that is, the net assets lying for a probable loss or possible profit on book value, the balance being available for shareholders included in the liabilities may be debentures, debenture interest, expenses outstanding and possible preference dividends if the articles of association stipulate for payment of shares in winding up.

However, although a balance sheet usually gives an accurate indication of short-term assets and liabilities. This is not the case of long-term ones as they may be hidden by techniques such as "off balance sheet financing". Moreover, a balance sheet is a historical record of previous expenditure and existing liabilities.

Answer to Question No. 6(ii)

Valuation for liquidation/insolvency

Net Realisable Value Method is generally used in case of liquidation. Where the business of the company is being liquidated, its assets have to be valued as if they were individually sold and not on a going concern basis. Liabilities are deducted from the liquidation value of the assets to determine the liquidation value of the business. One should also consider liabilities which will arise on closure such as retrenchment compensation, termination of critical contracts, etc. Tax consequences of liquidation should also be considered. Any distribution to the shareholders of the company on its liquidation, to the extent of accumulated profits of the company is regarded as deemed dividend. Dividend Distribution tax will have to be captured for such valuation.

Answer to Question No. 6(iii)

Market Comparable

Market comparable method is generally, applied in case of unlisted entities. This method estimates value by relating the same to underlying elements of similar companies for past years. It is based on market multiples of ‘comparable companies’. For example:

- Earnings/Revenue Multiples (Valuation of Pharmaceutical Brands)
- Book Value Multiples (Valuation of Financial Institution or Banks)
- Industry Specific Multiples (Valuation of cement companies based on Production capacities)
- Multiples from Recent M&A Transactions.
Though this method is easy to understand and quick to compute, it may not capture the intrinsic value and may give a distorted picture in case of short term volatility in the markets. There may often be difficulty in identifying the comparable companies.

**Question No. 7**

*Discuss about Income Tax Implication in the process of demerger.*  
(8 marks)

**Answer to Question No. 7**

As per Section 19AAA of the Income Tax Act, 1961, “demerged company” means the company whose undertaking is transferred, pursuant to a demerger, to a resulting company;

A demerger scheme usually involves the allotment of shares in the transferee company to the shareholders of the transferor company, in lieu of their reduction of their interest in the transferee company having a mirror image of shareholdings. If post demerger as part of strategy, intention is to create holding subsidiary relationship or retain part stake than it is possible to allot shares of the transferee company to the transferor company.

In the context of a demerger scheme, a valuation exercise is mandatory in order to determine the number of shares to be issued to the shareholders of the transferor company in consideration for the spin off/demerger of the undertaking or undertakings. If demerger is going to be in ‘Shell Company’, than valuation is primarily to determine the capital structure of the Transferee/Resultant Company.

If the demerged and resulting companies belong to same group of management and shareholders are common, share exchange ratio based on Net Asset Based valuation model may be adopted. Any other business valuation method may also be adopted considering the same shareholding as it will not impact value for the shareholders in demerged company post-demerger. In ideal situation like the companies are profitable and shareholders are different, it is recommendable to use Profit Based Valuation model for deciding on the share exchange ratio. While demerging to the shell company, there is no value of the shell company. Therefore, any no of shares may be issued to the shareholders of the demerged company as there will not be any impact on the shareholders' wealth.

There may be various situations and objectives wherein demerger schemes are implemented. Fair valuation only considers the status of the businesses and other macro factors but it also considers very big picture of implication of valuation/share exchange ratio. It does also consider costs such as stamp duty involved in adopting any valuation model.

**Question No. 8**

*Critically examined the Income Tax Implication involved in slump sale.*  
(7 marks)

**Answer to Question No. 8**

The concept of Slump Sale was incorporated in the Income tax Act, 1961 by the Finance Act, 1999 when Section 2(42C) was inserted defining the term ‘slump sale’ as transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities. Prior to the insertion
of Section 2(42C), Courts have held that slump sale is a sale of a business on a going concern basis where the lumpsum price cannot be attributed to individual assets or liabilities.

The undertaking has to be transferred as a result of sale. If an undertaking is transferred otherwise than by way of sale, say, by way of exchange, compulsory acquisition, extinguishment, inheritance by will, etc., the transaction may not be covered by Section 2(42C). The consideration for transfer is a lump sum consideration. This consideration should be arrived at without assigning values to individual assets and liabilities.

As regards the valuation of slump sale it is appropriate to brief the provisions of Section 50B of the Income Tax Act, 1961. Section 50B provides the mechanism for computation of capital gains arising on slump sale. Capital gains arising on slump sale are calculated as the difference between sale consideration and the net worth of the undertaking. Net worth is deemed to be the cost of acquisition and cost of improvement for the purpose of calculation of capital gains tax.

Net worth is defined in Explanation 1 to Section 50B as the difference between ‘the aggregate value of total assets of the undertaking or division’ and ‘the value of its liabilities as appearing in books of account’

The ‘aggregate value of total assets of the undertaking or division’ is the sum total of:

1. WDV as determined u/s.43(6)(c)(i)(C) in case of depreciable assets.
2. The book value in case of other assets.

**Part C (20 Marks)**

**Question No. 9**

(a) Though, UNCITRAL Model Law is not a substantive law, yet it recommends protection to creditors and other interested persons. Briefly describe what are the protections provided under the UNCITRAL Model Law.

(b) The main objective of Asset Reconstruction Company (ARC) is to act as an agent for banks and financial institutions. Briefly explain with the relevant provisions of law. (5 marks each)

**Answer to Question No. 9(a)**

UNCITRAL Model Law (hereinafter “the Model Law”) in its preamble mention that objects of the Model Law is not to create substantive rights but to give general orientation for users of the Model Law and to provide effective mechanism to deal with cross border insolvency.

Model Law contains following provisions for protection of the creditors, the debtors and other affected persons:

1. temporary relief upon application for recognition of a foreign proceeding or upon recognition, which is at the discretion of the Court, on being satisfied that interest of the creditors and other interested persons are adequately protected;
2. the court may grant relief subject to the conditions, as it thinks fit;
3. the Court may modify or terminate the relief granted, if so requested by a person affected thereby.

Model Law further provides that in case of actions are manifestly contrary to the public policy of the enacting state, the court may refuse taking any action under the Model Law.

Answer to Question No. 9(b)

Reconstruction company means a company incorporated under provisions of Companies Act, 1956 for purpose of assets reconstruction. The problem of non-performing loans created due to systematic banking crisis world over has become acute. Focused measures to help the banking systems to realise its NPAs has resulted into creation of specialised bodies called asset management companies which in India have been named asset reconstruction companies ('ARCs').

The main objective of asset reconstruction company ('ARC') is to act as agent for any bank or financial institution for the purpose of recovering their dues from the borrowers on payment of fees or charges, to act as manager of the borrowers' asset taken over by banks, or financial institution, to act as the receiver of properties of any bank or financial institution and to carry on such ancillary or incidental business with the prior approval of Reserve Bank wherever necessary. If an ARC carries on any business other than the business of asset reconstruction or securitisation or the business mentioned above, it shall cease to carry on any such business within one year of doing such other business.

Question No. 10

(a) As the Company Secretary of a company, mention your duties in respect of compulsory winding-up.

(b) Winding-up and dissolution are synonymous. Comment. (5 marks each)

Answer to Question No. 10(a)

The duties of the Secretary in respect of compulsory winding up of the company may be enumerated as follows:

(i) If the company itself makes the petition for compulsory winding up, the Secretary should help the directors in drawing up the petition.

(ii) He should see that a copy of winding up order, when passed by the Court is filed with the Registrar within 30 days of the making of the order.

(iii) He should help in preparation of the statement of affairs of the company in the prescribed form for submission to the Official Liquidator. He should see that it is properly verified by an affidavit.

(iv) He should give all necessary information to the Court, when called upon by it during the course of the winding up.

(v) He should see that all documents, correspondence etc., issued by the company during the period of winding up contain a statement that the company is being wound up.
The terms “Winding up” and “Dissolution” are sometimes erroneously used to mean the same thing. But according to the Companies Act, 1956, the legal implications of these two terms are quite different and there are fundamental differences between them as regards the legal procedure involved. The main points of distinction are given below:

1. The entire procedure for bringing about a lawful end to the life of a company is divided into two stages – ‘winding up’ and ‘dissolution’. Winding up is the first stage in the process whereby assets are realised, liabilities are paid off and the surplus, if any, distributed among its members. Dissolution is the final stage whereby the existence of the company is withdrawn by the law.

2. The liquidator appointed by the company or the Court carries out the winding up proceedings but the order for dissolution can be passed by the Court only.

3. According to the Companies Act the liquidator can represent the company in the process of winding up. This can be done till the order of dissolution is passed by the Court. Once the Court passes dissolution orders the liquidator can no longer represent the company.

4. Creditors can prove their debts in the winding up but not on the dissolution of the company.

5. Winding up in all cases does not culminate in dissolution. Even after paying all the creditors there may still be a surplus; company may earn profits during the course of beneficial winding up; there may be a scheme of compromise with creditors while company is in winding up and in all such events the company will in all probability come out of winding up and hand over back to shareholders/old management. Dissolution is an act which puts an end to the life of the company.

As such winding up is only a process while the dissolution puts an end to the existence of the company. Unless and until it has been set aside under Section 559 of the Act, it prevents any proceedings being taken against promoters, directors or officers of the company to recover money or property due or belonging to the company or to prove a debt due from the company. When the company is dissolved, the statutory duty of the liquidator towards the creditors and contributories is gone, but if he has committed without complying with the requirements of the Act, he is liable to damages to the creditors.